

# **STRENGTHENING ANTI-MONEY LAUNDERING SURVEILLANCE ALONGSIDE ADVANCEMENTS IN FINANCIAL TECHNOLOGY**

A Study of the Transaction Profile of Accredited Virtual Currency Exchanges in the Philippines



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## EXECUTIVE SUMMARY

On 6 February 2017, the BSP issued Circular No. 944 (Guidelines for VC Exchanges), establishing a formal regulatory framework for virtual currency (VC) exchanges. Under the said issuance, VC exchanges or businesses engaged in the exchange of VCs for equivalent fiat money in the Philippines are required to register with the BSP as remittance and transfer companies. This study was conducted to form a preliminary assessment of the transaction profile of accredited VC exchanges, particularly in relation to suspicious transactions, clients suspected of links to illicit activities, and big-ticket transactions.

This study performs descriptive analysis on Covered Transaction Reports (CTRs) and Suspicious Transaction Reports (STRs) received from BSP-accredited VC exchanges from 6 March 2017 to 10 April 2018, which involved transactions executed on their platforms from 28 April 2014 to 6 April 2018, yielding a total of 22,366 transaction reports (composed of 1,086 CTRs and 21,280 STRs) with a combined value of PHP3.1 billion (PHP2.4 billion are CTRs and PHP0.7 billion are STRs). Based on these data, transactions were grouped according to type (i.e., CTR and STR), year, and reporting entity. The analysis was then shifted to the STRs, with entries classified according to the entities' characterization of suspicious activities and then distributed according to transactional value. Based on the transaction codes entered by the entities, the nature of these transactions were also studied. A breakdown of the CTRs by year and transaction type was likewise examined.

Following the BSP's issuance of Circular No. 944 in February 2017 and subsequent approval of the registration of Betur, Inc. and Rebittance, Inc. in September and October 2017 respectively, VC exchange-reported transactions increased dramatically in both volume and value for 2017. Total volume increased by 170% (driven by 161% and 845% growth in STRs and CTRs, respectively) while total value increased by 608% to reach an aggregate amount of PHP1.7 billion.

Bulk of the total number of STRs (at 41.9%) were tagged as deviations from the clients' profile and/or transaction history, including transaction amounts not commensurate with one's financial capacity. Aside from such reasons relating to doubts on the clients' profile and/or nature of transactions, the 3 most frequently cited reasons for suspicion or circumstances warranting the filing of STRs all shared links to investment fraud, such as participation in (1) investment schemes, (2) swindling, and (3) fraudulent practices and other violations under The Securities Regulations Code of 2000. Taken together, these account for 6,670 STRs amounting to PHP121.8 million (equivalent to 31.3% of the total volume and 18.5% of the total value of STRs).

Most suspicious transactions reported by the VC exchanges are smaller ticket items, with 95.7% of the sample consisting of amounts below PHP100,000. Nonetheless, despite the volume of STRs from the smallest bracket of PHP 1 - 9,999 (at 9,231 transactions or 43.4% of total), these account for only 4.6% of the total value of transactions. On the other hand, while STRs belonging to the PHP 100,000 - 499,999 bracket comprise 4.2% of the total in terms of volume, these account for the largest aggregate value, at 35.7% of total.

In terms of volume, suspicious transactions were mostly outward remittances to domestic beneficiaries (comprising 59.4% of total volume), while the rest were in the form of cash deposits (comprising 40.6% of total volume). On the other hand, the reverse can be said about the composition of suspicious transactions in terms of value, where cash deposits dominate at 58.5% of total, while the remaining 41.5% of transactions are composed of different forms of domestic outward remittances.

Similar to STR data, domestic outward remittances comprised majority of covered transactions in terms of volume (at 55.4% of total), whereas cash deposits formed a larger portion in terms of value (at 59.1% of total). Examining monthly data, a surge in cash deposits was noted for December 2017, amounting to PHP147.0 million or 22.0% of total cash deposits for the year.

The VC exchange industry's reports on suspicious transactions, consumer behavior, and account holders have shed light on various methods and techniques employed by criminals to usurp money from unsuspecting victims and/or launder the proceeds of illicit activities. The recurring element of fraud among the identified schemes may warrant enhanced monitoring and implementation of more stringent preventive measures in this aspect. The main suspicious trigger gleaned from the reports is an unusually high volume of fund inflows (via cash deposits and/or incoming transfers from other VC platform users) and/or outflows (typically via outgoing transfers to external VC wallets or conversion to cash).

The establishment of a regulatory framework for VC exchanges has strengthened safeguards against money laundering and terrorist financing and has allowed for more comprehensive monitoring of the financial behavior of individuals and entities possibly connected to illicit activities as well as closer coordination and information sharing among Covered Persons (CPs) in the conduct of AML surveillance. Nonetheless, the strengthening of entities' internal AML controls, conduct of public information programs, and passage of legislations enhancing individual identification systems would aid in tracking down criminals and curbing illicit activities.

## I. INTRODUCTION

Virtual Currency (VC), as defined by the BSP, refers to any type of digital unit that is used as a medium of exchange or a form of digitally stored value created by agreement within the community of VC users.<sup>1</sup> Its electronic nature allows VCs to facilitate the movement of funds at a faster, cheaper, and more convenient manner compared to traditional remittance and payment channels, which accrues benefits in areas such as (1) remittances and wire transfers, (2) electronic payments, and (3) financial inclusion.<sup>2</sup> Nonetheless, with the potential benefits are attendant risks, especially as VCs offer a high degree of anonymity which may be exploited for money laundering and other unlawful activities.<sup>3</sup>

### ***Regulatory Frameworks across Jurisdictions<sup>4</sup>***

The global regulatory environment for VCs has been marked by disparity, with regulatory response ranging from the introduction of a licensing system for digital-asset exchanges in Japan to an outright ban on digital-asset exchanges and initial coin offerings (ICOs), as is the case in China.

An article published in Bloomberg on 20 March 2018 illustrates a cross-country comparison of the policy stances taken by different governments around the world with regard to VCs, as seen in Figure 1.

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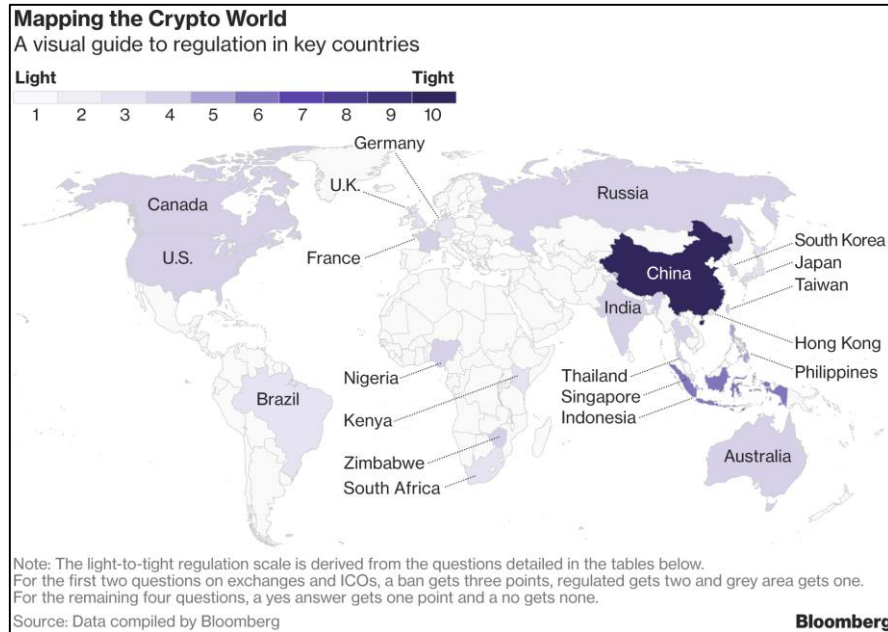
<sup>1</sup> BSP Circular No. 944: "Guidelines for Virtual Currency (VC) Exchanges" issued on 6 February 2017

<sup>2</sup> [www.bsp.gov.ph/downloads/Publications/FAQs/VC.pdf](http://www.bsp.gov.ph/downloads/Publications/FAQs/VC.pdf)

<sup>3</sup> <http://www.bsp.gov.ph/publications/media.asp?id=3377>

<sup>4</sup> <https://www.bloomberg.com/news/articles/2018-03-19/is-this-legal-making-sense-of-the-world-s-cryptocurrency-rules>

**Figure 1. Mapping of Cryptocurrency Policy Stances of Different Countries**



Source: "Making Sense of the World's Cryptocurrency Rules", Bloomberg (20 March 2018)

Of the countries included in the Bloomberg study, only Japan and the Philippines were noted to have already put in place regulations for VC exchanges while most economies including the US, UK, Germany, Hong Kong, Taiwan, and Singapore have adopted a more hands-off/wait-and-see approach and have not taken concrete policy stances as of writing. Nonetheless, other economies have begun to address gray areas with regard to VCs as South Korea has begun working on a comprehensive set of regulations while the European Commission is in the process of reviewing the bloc's regulatory framework for VCs. Only China, which used to be a hub for cryptocurrency trading, has taken an adverse stance against VCs, prohibiting digital-asset exchanges and ICOs, blocking online access to overseas trading platforms, and cutting off power to Bitcoin miners.

Vietnam has also taken a strong stance against cryptocurrencies, with authorities issuing pronouncements that all cryptocurrencies and transactions in cryptocurrencies are illegal in Vietnam.<sup>5</sup> The country has recently found itself embroiled in the middle of a \$658-million cryptocurrency scam involving a fraudulent ICO by a company in Ho Chi Minh City, wherein investors were seeing the value of their purchased tokens increase within the platforms' systems but were unable to withdraw their profits. Following the incident, authorities have called for greater vigilance against cryptocurrency transactions and investments and reiterated their stance against cryptocurrencies.<sup>6</sup> India and Pakistan have likewise banned regulated entities from dealing with cryptocurrencies in their countries.<sup>7</sup>

### **The Philippine Case**

In his speech at the Chamber of Thrift Banks' Annual Convention on 10 April 2018, BSP Governor Nestor A. Espenilla, Jr. called the "digital transformation of the financial services industry [as] the new frontier".<sup>8</sup> In a country where Overseas Filipinos' (OF) cash remittances represent 9.0% of GDP<sup>9</sup> and

<sup>5</sup> <https://www.reuters.com/article/vietnam-cryptocurrency/vietnam-calls-for-tougher-measures-on-cryptocurrency-deals-amid-alleged-scam-idUSL3N1RO4DL>

<sup>6</sup> <http://fortune.com/2018/04/12/icos-cryptocurrency-scam-vietnam/>

<sup>7</sup> [www.bbc.com/news/world-asia-india-43669730](http://www.bbc.com/news/world-asia-india-43669730); <https://tribune.com.pk/story/1679446/2-pakistan-bans-cryptocurrencies/>

<sup>8</sup> "Navigating the Digital Frontier". Speech made by Gov. Nestor Espenilla, Jr. at the Chamber of Thrift Banks Annual Convention, 10 April 2018, Makati Shangri-La Hotel. (<http://www.bsp.gov.ph/publications/speeches.asp?id=60>)

<sup>9</sup> Based on full-year 2017 data

34.5% of cities and municipalities remain unbanked and 9.8% remain without any financial access point,<sup>10</sup> VCs could pave the way for alternative financial touchpoints. With this, the BSP recognizes the growth opportunities from financial technology (fintech) innovations and has employed a ‘test and learn’ approach or regulatory sandbox to allow innovations to flourish while mitigating the effects of technology-related risks and promoting financial integrity, transparency in financial transactions, and consumer protection.<sup>11</sup> This is the same approach used in 2004 leading to the successful development of electronic money (Smart Money and GCash) in the Philippines. BSP’s approach includes: 1) allowing the market to develop and innovations to take place; 2) proceeding with flexibility yet with caution; 3) understanding operating/business models; 4) using existing regulations and adopting the appropriate regulatory approach based on experience and lessons learned; and 5) closely monitoring developments and settling issues that may arise.

The increasing use of VC in the Philippines, whether as a medium for payment or remittance, has prompted the BSP to issue/adopt the following advisories, policies, and regulations:

- (1) As early as 2014 when VCs were starting to grow in the Philippine market, the BSP issued an advisory to inform the public of the features, benefits, and attendant risks when dealing with VCs.<sup>12</sup>
- (2) On 20 January 2017, the BSP issued Circular 942 creating an enhanced regulatory framework for pawnshops and money service business (MSBs) to ensure that even non-banks are properly supervised for effective compliance with AML and internal control rules and guidelines.<sup>13</sup>
- (3) On 6 February 2017, the BSP issued Circular 944, establishing a formal regulatory framework for VC exchanges. Under the said issuance, VC exchanges or businesses engaged in the exchange of VCs for equivalent fiat money in the Philippines are required to register with the BSP as remittance and transfer companies. In view thereof, BSP-registered VC exchanges are now required to put in place adequate safeguards to address the risks associated with VCs such as basic controls on anti-money laundering and terrorist financing, technology risk management, and consumer protection. Notwithstanding said issuance, the BSP does not, in any way, endorse VCs as legal tender, store of value, or an investment vehicle.<sup>14</sup>
- (4) In December 2017, the BSP issued another public advisory in response to certain unscrupulous fraudsters/groups that try to entice consumers to “invest” in Bitcoins or VCs packaged as an ICO. The advisory warned consumers to be cautious in dealing with VCs, only maintain VCs sufficient to meet their transactional requirements, and adopt sound security measures to protect their VC accounts. The advisory also reiterated that BSP does not endorse VCs as a currency or an investment instrument due to its highly speculative and risky nature.<sup>15</sup>

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<sup>10</sup> As of 3Q 2017, out of the 1,071 cities and municipalities in the country, 563 remain unbanked, i.e.: without banking presence, while 160 remain without any financial access point. (Source: BSP’s Philippine Financial Inclusion Dashboard as of 3Q 2017)

<sup>11</sup> “Navigating the Digital Frontier”. Speech made by Gov. Nestor Espenilla, Jr. at the Chamber of Thrift Banks Annual Convention, 10 April 2018, Makati Shangri-La Hotel. (<http://www.bsp.gov.ph/publications/speeches.asp?id=60>)

<sup>12</sup> <https://www.philstar.com/business/2018/04/09/1804063/bsp-evaluating-applications-virtual-currency-exchanges#zscRtvXjPwWkYyXp.99>

<sup>13</sup> <http://www.bsp.gov.ph/publications/speeches.asp?id=589>

<sup>14</sup> [www.bsp.gov.ph/downloads/Publications/FAQs/VC.pdf](http://www.bsp.gov.ph/downloads/Publications/FAQs/VC.pdf)

<sup>15</sup> Ibid.

The adoption of VC as an investment vehicle, as a crowdfunding tool, and even as a mode for perpetrating investment scams has led the Securities and Exchange Commission (SEC) to issue the following advisories:<sup>16</sup>

- (1) On 8 January 2018, the SEC issued a warning to the public in light of companies/individuals soliciting investments for unregistered ICOs. The advisory stated that VC issuances satisfying the definition of securities as set out in the Securities Regulation Code (SRC) are covered under the jurisdiction of the SEC and consequently would require registration.<sup>17</sup> The advisory also warned that the sale and offer of unregistered securities are illegal and will be penalized under the SRC.<sup>18</sup>
- (2) On 10 April 2018, the SEC issued a warning against investment schemes in cloud mining contracts, where investors would fund the purchase of equipment used in cryptocurrency mining in exchange for a share in the proceeds of the mining activity. The advisory asserted that cloud mining contracts are investment contracts falling within the purview of the term “securities” as defined by law and are thus covered by the SEC. In view thereof, unregistered investment taking involving such contracts will be subject to criminal sanctions.<sup>19</sup>

The SEC has also taken regulatory actions against specific entities engaged in illegal VC-related investment activities, which will be discussed in detail in Section V (Cases involving VC Exchanges).

### ***VC Exchanges in the Philippines***

As defined in BSP Circular 944, VC exchange refers to an entity that offers services or engages in activities that provide facility for the conversion or exchange of fiat currency to VC or vice versa. Duly registered VC exchanges may perform other money or value transfer services such as the acceptance of cash, checks, and other monetary instruments, and/or payment to a beneficiary by means of a communication, message, transfer, or through a clearing network. Currently, there are 2 operating BSP-registered VC exchanges: Betur, Inc. and Rebittance, Inc., which were accredited in September and October 2017, respectively. The industry is set to expand further on the back of BSP’s recent pronouncements that is currently evaluating the applications of 29 companies planning to set up VC exchanges in the country.<sup>20</sup>

- (1) Betur, Inc., a subsidiary of Singapore-based e-commerce applications developer Global Commerce Technologies Pte. Ltd.<sup>21</sup>, is a remittance agent offering cash-in and cash-out services, mobile airtime top-ups, remittance services, bill payments, and VC exchange under the Coins.ph brand.<sup>22</sup> Coins.ph is a mobile blockchain-enabled platform operating in the Philippines and Thailand that provides customers access to a mobile wallet and services such as remittances, air-time, bill payments, and online shopping at over 100,000 merchants which accept digital currency.<sup>23</sup>

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<sup>16</sup> Note: Subsequent to the study’s reference date of 12 April 2018, the SEC issued an advisory dated 18 April 2018 warning the public against investing in internet-based bitcoin and cryptocurrency Ponzi schemes. The advisory also included a list of red flags that the public must watch out for in order to avoid being victimized by scammers.

Source: [https://www.sec.gov.ph/wp-content/uploads/2018/04/2018Advisory\\_WarningOnBitcoin\\_Related\\_Ponzi.pdf](https://www.sec.gov.ph/wp-content/uploads/2018/04/2018Advisory_WarningOnBitcoin_Related_Ponzi.pdf), accessed on 8 August 2018.

<sup>17</sup> Section 3.1 of the SRC defines securities as “shares, participation or interests in a corporation or in a commercial enterprise or profit-making venture and evidenced by a certificate, contract, instrument, whether written or electronic in character”.

<sup>18</sup> <https://www.sec.gov.ph/sec-advisory-on-initial-coin-offerings/>

<sup>19</sup> <http://www.sec.gov.ph/advisory-on-cloud-mining-contracts/>

<sup>20</sup> <https://www.philstar.com/business/2018/04/09/1804063/bsp-evaluating-applications-virtual-currency-exchanges#zscRtvXjPwWkYyXp.99>

<sup>21</sup> <https://opencorpdata.com/sg/201422482H>

<sup>22</sup> <https://coins.ph/user-agreement/>

<sup>23</sup> <https://coins.ph/about>

- (2) Rebitance, Inc., a subsidiary of Philippine fintech company Satoshi Citadel Industries (SCI) Ventures, Inc., provides remittance services, cross-border payments, payroll services, bills payments, and top-up of mobile load.<sup>24</sup>

In view of the expansion of the VC exchange industry in the Philippines, this study aims to conduct a preliminary assessment of the transaction profile of BSP-registered VC exchanges, as these transactions relate to anti-money laundering efforts. For this purpose, the Covered Transaction Reports (CTRs) and Suspicious Transaction Reports (STRs) submitted by such entities will be used.

## II. METHODOLOGY

This study performs descriptive analysis on CTRs and STRs submitted by BSP-accredited VC exchanges from 6 March 2017 to 10 April 2018. The dataset covers transactions executed from 28 April 2014 to 6 April 2018, yielding a total of 1,086 CTRs and 21,280 STRs. To facilitate analysis and for comparability, transaction dates were converted to transaction years and the Philippine Peso (PHP) was used as reference currency across the entire dataset.

Financial intelligence analysts first studied the total volume and value of reported transactions by type (i.e., CTR and STR), year, and reporting entity. In order to make a rough comparison of the 2018 year-to-date data with 2017 full-year data, simple monthly averages were taken for the respective aggregate figures.

Analysts then proceeded to zero in on the STRs and reviewed the characterization of suspicious activities in these STRs and classified the transactions accordingly based on the reason and narrative indicated for each. The distribution of STR amounts was also assessed via the grouping of the transactions into ranges set by the analysts. Based on the transaction codes entered by the entities, the nature of these transactions were subsequently studied. A breakdown of the CTRs by year and transaction type was likewise examined.

Based on the analysis of the STRs, analysts identified typologies and indicators related to characterizations of suspicious activities.

## III. DATA AND STATISTICS

**Table 1. VC Exchange-Reported Transactions by Type<sup>25</sup>**

Transaction Year	CTR		STR		Total	
	Volume	Value*	Volume	Value*	Volume	Value*
2014			10	1.9	10	1.9
2015			78	1.0	78	1.0
2016	74	175.8	5,583	67.1	5,657	242.9
2017	699	1,189.5	14,550	531.5	15,249	1,721.0
2018**	313	1,031.7	1,059	57.1	1,372	1,088.8
<b>Total</b>	<b>1,086</b>	<b>2,396.9</b>	<b>21,280</b>	<b>658.7</b>	<b>22,366</b>	<b>3,055.6</b>

\*Values are in PHP million

\*\*Coverage of 2018 data is until 6 April 2018

<sup>24</sup> <https://sci.ph/rebit.html>

<sup>25</sup> The VC exchanges began submitting CTRs and STRs in 2017. Since STR submission hinges on the determination of the suspicious nature of a specific transaction regardless of the date it was executed, some reported transactions covered in the dataset were carried out on the VC exchanges' platforms in previous years (i.e., starting 2014).



Following the BSP's issuance of Circular No. 944 (Guidelines for VC Exchanges) in February 2017 and subsequent approval of the registration of Betur, Inc. and Rebittance, Inc. in September and October 2017 respectively, VC exchange-reported transactions increased dramatically in both volume and value for 2017. Total volume increased by 170% year-on-year (driven by 161% and 845% growth in STRs and CTRs, respectively) while total value increased by 608% year-on-year to reach an aggregate amount of PHP1.7 billion.

While accreditation for VC exchanges commenced in 2017, it may be observed that transactions executed using the said platform date back to 2014. At that time, VC exchanges could register their remittance business with the BSP under Circular No. 471 (Rules and Regulations for Foreign Exchange Dealers, Money Changers, and Remittance Agents) issued on 24 January 2005. Becoming duly registered remittance agents (RAs) would allow them to open bank accounts.

The narratives for some transactions were also noted to demonstrate a degree of coordination between the VC exchanges and other Covered Persons (such as correspondent banks), which has aided the former in identifying suspicious individuals and transactions. These may be indicative of proactive AML investigation and robust controls on the part of the regulated entities. Inter-entity coordination and knowledge sharing would also strengthen the capacity of the broader financial system in detecting and countering money laundering and terrorist financing.

**Table 2. Estimated Average Monthly Reported Transactions<sup>26</sup>**

Transaction Year	CTR		STR		Total	
	Volume	Value*	Volume	Value*	Volume	Value*
2017	58.3	99.1	1,212.5	44.3	<b>1,270.8</b>	<b>143.4</b>
2018**	104.3	343.9	353.0	19.0	<b>457.3</b>	<b>362.9</b>

\*Values are in PHP million

\*\*Coverage of 2018 data is until 6 April 2018

While full year information for 2018 has yet to be obtained, a rough estimate of the average monthly volume and value of reported transactions based on latest statistics indicates a significant decrease in volume (at 457.3, compared to the 2017 average of 1,270.8) despite a considerable increase in value (at PHP362.9 million, compared to the 2017 average of PHP143.4 million). While CTRs have increased both in volume and value, STRs have dramatically declined both in volume and value, thereby dragging on the statistics for 2018 so far. Notwithstanding, the implications of these observed year-on-year changes are not immediately apparent and may require further analysis, as these may be brought about by a confluence of factors such as the seasonality of remittances and/or transactions, heightened volatility of the price of bitcoin in late 2017 and its subsequent plunge, or a possible enhancement in the institutions' due diligence measures or AML control systems.

<sup>26</sup> To preliminarily estimate the monthly volume and value of transactions, extracted figures for 2017 were divided by 12 (months) while latest figures for 2018 were divided by 3 as the most recent reported transaction is dated 6 April 2018. Nonetheless, it must be emphasized that this is a rough computation and should not be interpreted as a definite trend indicator as it does not take into account factors such as seasonality of remittances/transactions.

**Table 3. Classification of STR Reasons\***

STR Classification	Volume		Value	
	Number	Share to Total	Amount (in PHP)	Share to Total
Deviation from Client's Profile/Past Transactions	4,912	23.1%	276,041,614.54	41.9%
No Underlying Legal or Trade Obligation, Purpose, or Economic Justification	4,880	22.9%	213,908,988.33	32.5%
Reason Not Immediately Identified <sup>27</sup>	3,693	17.4%	15,047,923.50	2.3%
Investment Scheme	3,684	17.3%	19,661,581.38	3.0%
Swindling	1,557	7.3%	37,355,922.09	5.7%
Fraudulent Practices and Other Violations under The Securities Regulations Code of 2000	1,429	6.7%	64,765,965.13	9.8%
Cybercrime	412	1.9%	23,775,602.03	3.6%
Robbery & Extortion	306	1.4%	2,990,065.03	0.5%
Client Not Properly Identified	123	0.6%	1,423,671.71	0.2%
Shopping Fraud	69	0.3%	427,159.60	0.1%
Violation of VC Exchange Policy	59	0.3%	818,284.68	0.1%
Frauds and Illegal Exactions and Transactions	51	0.2%	201,349.64	0.0%
Gambling	50	0.2%	1,158,627.41	0.2%
Unexplainable Source of Funds	24	0.1%	538,862.68	0.1%
Fraud	7	0.0329%	17,499.00	0.0027%
Intellectual Property Infringement	6	0.0282%	26,760.06	0.0041%
Child Abuse/Exploitation/Discrimination	5	0.0235%	142,741.00	0.0217%
Felonies	3	0.0141%	150,000.00	0.0228%
Gambling; Investment Scheme	3	0.0141%	111,500.00	0.0169%
Qualified Theft	2	0.0094%	40,124.00	0.0061%
Forgeries and Counterfeiting	1	0.0047%	20,000.00	0.0030%
Online Dating Fraud	1	0.0047%	1,000.00	0.0002%
Plunder	1	0.0047%	20,400.00	0.0031%
Smuggling	1	0.0047%	50,000.00	0.0076%
Transaction With High Level Politically Exposed Individual	1	0.0047%	21.00	0.000003%
<b>Total</b>	<b>21,280</b>	<b>100.0%</b>	<b>658,695,662.8</b>	<b>100.0%</b>

\* Transactions dated 28 April 2014 – 25 March 2018

Bulk of the total number of STRs (at 41.9%) were tagged as deviations from the clients' profile and/or transaction history, including transaction amounts not commensurate with one's financial capacity. Aside from such reasons relating to doubts on the clients' profile and/or nature of transactions, the 3 most frequently cited reasons for suspicion or circumstances warranting the filing of STRs all shared links to investment fraud, such as participation in (1) investment schemes, (2) swindling, and (3) fraudulent practices and other violations under The Securities Regulations Code of 2000. Taken together, these account for 6,670 STRs amounting to PHP121.8 million (equivalent to 31.3% of the total volume and 18.5% of the total value of STRs).

<sup>27</sup> These are STRs wherein the Reason for Suspicion supplied is "THE TRANSACTION IS SIMILAR, ANALOGOUS OR IDENTICAL TO ANY OF THE FOREGOING", without disclosing any further details on the transaction.

**Table 4. Distribution of STR Amounts (in terms of volume)**

Transaction Amount	Volume							
	2014	2015	2016	2017	2018	Total		
PHP 9,999 and below		47	4,767	4,322	95	9,231	43.4%	
PHP 10,000 - 49,999	3	28	517	5,873	337	6,758	31.8%	
PHP 50,000 - 99,999	2	3	169	3,646	565	4,385	20.6%	
PHP 100,000 - 499,999	4		128	705	62	899	4.2%	
PHP 500,000 - 999,999	1		2	2		5	0.0%	
PHP 1,000,000 and above				2		2	0.0%	
<b>Total</b>	<b>10</b>	<b>78</b>	<b>5,583</b>	<b>14,550</b>	<b>1,059</b>	<b>21,280</b>	<b>100.0%</b>	

**Table 5. Distribution of STR Amounts (in terms of total value)**

Transaction Amount	Value (in PHP million)							
	2014	2015	2016	2017	2018	Total		
PHP 9,999 and below		0.2	13.2	16.7	0.3	30.4	4.6%	
PHP 10,000 - 49,999	0.1	0.6	13.2	133.9	9.4	157.3	23.9%	
PHP 50,000 - 99,999	0.2	0.2	9.9	187.6	28.5	226.3	34.4%	
PHP 100,000 - 499,999	0.9		29.8	185.6	18.9	235.2	35.7%	
PHP 500,000 - 999,999	0.7		1.1	1.1		2.9	0.4%	
PHP 1,000,000 and above				6.6		6.6	1.0%	
<b>Total</b>	<b>1.9</b>	<b>1.0</b>	<b>67.1</b>	<b>531.5</b>	<b>57.1</b>	<b>658.7</b>	<b>100.0%</b>	

Most suspicious transactions reported by the VC exchanges are smaller ticket items, with 95.7% of the sample amounting to below PHP100,000. Nonetheless, despite the volume of STRs from the smallest bracket of PHP 1 - 9,999 (at 9,231 transactions or 43.4% of total), these account for only 4.6% of the total value of transactions. On the other hand, while STRs belonging to the PHP 100,000 - 499,999 bracket comprise 4.2% of the total in terms of volume, these account for the largest aggregate value, at 35.7% of total.

To date, 7 transactions exceeding PHP500,000 have been identified as suspicious, with reasons as follows: (1) association of account owner with online gambling; (2) account owner suspected to be in violation of the Cybercrime Prevention Act of 2012; and (3) no established legal/trade purpose nor economic justification for the transactions involved.

**Table 6. STR Volume by Transaction Type**

	2014	2015	2016	2017	2018	Total	
<b>Deposit - Cash</b>	10	33	453	7,451	692	8,639	40.6%
<b>Outward Remittance (Domestic)</b>		45	5,130	7,098	367	12,640	59.4%
<i>For Further Credit to Another Account</i>			2,486	1,178		3,664	17.2%
<i>Credit to Beneficiary's Account</i>		23	2,472	3,511	92	6,098	28.7%
<i>Payment to Beneficiary in Cash</i>		22	172	2,409	275	2,878	13.5%
<b>STR Transaction<sup>28</sup></b>				1		1	0.0%
<b>Total</b>	<b>10</b>	<b>78</b>	<b>5,583</b>	<b>14,550</b>	<b>1,059</b>	<b>21,280</b>	<b>100.0%</b>

<sup>28</sup> The sole STR transaction under consideration may have been incorrectly tagged as such, given that the transaction narrative indicates that the account holder received PHP1.1 million pesos from an external wallet but could not provide sufficient details on the source of the funds. The source account was later found to have been previously reported for a scam case.

**Table 7. STR Value by Transaction Type (in PHP million)**

	2014	2015	2016	2017	2018	Total	
<b>Deposit - Cash</b>	1.9	0.7	17.8	325.7	38.9	<b>385.1</b>	<b>58.5%</b>
<b>Outward Remittance (Domestic)</b>		0.3	49.3	205.8	18.2	<b>273.6</b>	<b>41.5%</b>
<i>For Further Credit to Another Account</i>			8.3	4.2		<i>12.5</i>	<i>1.9%</i>
<i>Credit to Beneficiary's Account</i>		0.2	38.9	147.9	11.4	<i>198.5</i>	<i>30.1%</i>
<i>Payment to Beneficiary in Cash</i>		0.1	2.1	53.7	6.7	<i>62.7</i>	<i>9.5%</i>
<b>STR Transaction<sup>29</sup></b>				0.0		<b>0.0</b>	<b>0.0%</b>
<b>Total</b>	<b>1.9</b>	<b>1.0</b>	<b>67.1</b>	<b>531.5</b>	<b>57.1</b>	<b>658.7</b>	<b>100.0%</b>

In terms of volume, suspicious transactions were mostly outward remittance to domestic beneficiaries (comprising 59.4% of total volume), while the rest were in the form of cash deposits (comprising 40.6% of total volume) and 1 tagged as an STR transaction (which may have been erroneously tagged as such, as pointed out in footnote 28). On the other hand, the reverse can be said about the composition of suspicious transactions in terms of value, where cash deposits dominate at 58.5% of total, whereas the remaining 41.5% of transactions are composed of different forms of domestic outward remittances.

It can be observed that the volume and value of cash deposits tagged as suspicious have increased significantly in 2017, although these appear to have decreased in 2018 thus far. Examining monthly data, large cash deposit flows were noted for September to December 2017, amounting to PHP237.7 million or 73.0% of total cash deposit STRs for the year. The large inflow of cash deposits was observed to continue to January 2018, which accounted for PHP32.0 million or 82.1% of the total value of cash deposit STRs reported year-to-date.

**Table 8. CTR Volume by Transaction Type**

	2016	2017	2018	Total	
<b>Deposit - Cash</b>	47	226	173	<b>446</b>	<b>41.1%</b>
<b>Outward Remittance (Domestic)</b>	27	473	102	<b>602</b>	<b>55.4%</b>
<i>For Further Credit to Another Account</i>		1		<i>1</i>	<i>0.1%</i>
<i>Credit to Beneficiary's Account</i>		430	102	<i>532</i>	<i>49.0%</i>
<i>Payment to Beneficiary in Cash</i>	27	42		<i>69</i>	<i>6.4%</i>
<b>Inward Remittance (Domestic): Credit to Beneficiary's Account</b>			38	<b>38</b>	<b>3.5%</b>
<b>Total</b>	<b>74</b>	<b>699</b>	<b>313</b>	<b>1,086</b>	<b>100.0%</b>

**Table 9. CTR Value by Transaction Type (in PHP million)**

	2016	2017	2018	Total	
<b>Deposit - Cash</b>	154.2	667.5	593.7	<b>1,415.5</b>	<b>59.1%</b>
<b>Outward Remittance (Domestic)</b>	21.5	521.9	267.1	<b>810.6</b>	<b>33.8%</b>
<i>For Further Credit to Another Account</i>		1.2		<i>1.2</i>	<i>0.0%</i>
<i>Credit to Beneficiary's Account</i>		483.3	267.1	<i>750.4</i>	<i>31.3%</i>
<i>Payment to Beneficiary in Cash</i>	21.5	37.5		<i>59.0</i>	<i>2.5%</i>
<b>Inward Remittance (Domestic): Credit to Beneficiary's Account</b>			170.9	<b>170.9</b>	<b>7.1%</b>
<b>Total</b>	<b>175.8</b>	<b>1,189.5</b>	<b>1,031.7</b>	<b>2,396.9</b>	<b>100.0%</b>

<sup>29</sup> Please see previous footnote.

Similar to STR data, domestic outward remittances comprised majority of covered transactions in terms of volume (at 55.4% of total), whereas cash deposits formed a larger portion in terms of value (at 59.1% of total). Examining monthly data, a surge in cash deposits was noted for December 2017, amounting to PHP147.0 million or 22.0% of total cash deposits for the year.

#### **IV. TYPOLOGIES AND INDICATORS**

The VC exchanges' reports on suspicious transactions, consumer behavior, and account holders have shed light on various methods and techniques employed by criminals to usurp money from unsuspecting victims and/or launder the proceeds of illicit activities. A key element noted in the execution of such unlawful activities is anonymity, whether through means such as the extraction of funds in cash in order to remove the money trail or the usage of an untraceable mobile sim to be able to assume a fake identity in withdrawing funds. In particular, recurring schemes that may warrant enhanced monitoring and implementation of more stringent preventive measures include:

- **Unlicensed Investment Scheme**

The perpetrator uses an account in the VC platform to solicit funds for an unlicensed investment scheme. The victim opens an account in the VC platform or performs over-the-counter cash deposits to transfer money to the wallet address provided by the perpetrator. At first, the gains on the investment are delivered as promised, and the victim is encouraged to top up on the investment and refer more members in order to earn commissions. Eventually, an issue arises which allegedly causes the perpetrator to fail to deliver the funds as promised. Communication subsequently ceases and victims are unable to contact the perpetrator through all available channels. The perpetrator deliberately severs all connections – deactivating groups and pages, blocking the victim's account, and the like.

- **Online Shopping Fraud**

The perpetrator poses as a seller of products/services in social media channels or online shopping sites, requiring a payment to an account within the VC platform prior to delivery of items. After the payment is made, the perpetrator promptly cuts all communication with the victim and removes/deactivates all social media connections. Delivery of the promised product/service is never fulfilled.

- **Identity Theft**

The perpetrator assumes the identity of a legitimate online store and sells items on the internet similar to those being sold by the online store, advising the victim – a prospective customer – to remit payments to an account in the VC platform prior to shipment of the purchased items. Payments are immediately withdrawn from the account and all communication with the victim is cut.

- **Identity Theft**

The perpetrator deceives a victim by pretending to be the victim's relative and then requests for money through a payment center, possibly through a VC platform.

- **Unauthorized Withdrawal via Cybercrime**

The perpetrator accesses a client's account without authorization via online means such as hacking or phishing and then withdraws the funds in cash through the VC platform's payment partner using a fabricated identity, effectively eliminating the money trail.

- **Fraud (with Claims of Hacking of the Suspect's Account)**

The victim is contacted by an acquaintance (in this particular case, a colleague) asking if there is a nearby payment center to the victim and subsequently seeks assistance in making payments/deposits to particular reference numbers, promising to pay off the debt as soon as they meet. However, after completion of the transaction, the acquaintance claims that the account was hacked.

- **Fraud (via Exploitation of System Glitch)**

The perpetrator avails the services of a VC platform's payment partner then exploits a glitch in its system wherein simultaneously triggering a credit in one's account and cashing out funds would result in an erroneous credit to one's account.

- **Advance Fee Fraud**

The victim comes across a post on social media where the perpetrator, who claims to be part of a capital financing company, advertises loan offerings for additional capital (possibly targeting small-time entrepreneurs). The victim avails of the loan and is told that in order for the loan to be released, a processing fee must first be paid. The victim can no longer contact the perpetrator after payment of the processing fee.

- **Online Dating Fraud**

The victim and perpetrator meet in a dating site and eventually agree to meet up at a particular place and time. The victim shoulders the transportation allowance of the perpetrator but is unable to communicate with the perpetrator subsequent to the deposit of funds.

#### **WARNING INDICATORS**

- Unusually high volume of fund inflows (via cash deposits and/or incoming transfers from other VC platform users) and/or outflows (typically via outgoing transfers to external VC wallets or conversion to cash)
- Multiple person-to-person (P2P) transfers from various accounts within the VC exchange
- Immediate turnover of newly received funds
- Attempts to purchase verified accounts within the VC platform

## **V. CASES INVOLVING VIRTUAL CURRENCIES<sup>30</sup>**

**Bitcoin Scam.** An individual used his company originally registered as a sole proprietorship under a different purpose to operate a pyramid scheme using VC bitcoin as a front to explain the company's source of earnings and VC exchange platforms to facilitate payments and investments. Under the scheme, investors were promised double-digit interest rates every few weeks. As the suspects resorted to pyramiding and employed middlemen to serve as recruiters of new investors, the scheme's geographical reach extended nationwide. The perpetrators were eventually arrested. Months prior to

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<sup>30</sup> Note: Subsequent to the study's reference date of 12 April 2018, the SEC issued advisories warning the public against investing in 14 unregistered internet-based investment schemes and 1 unregistered entity that recently launched an unlicensed ICO.

- The internet-based investment schemes employed similar operations, such as: (1) offering investment contracts on social media; (2) offering unrealistic returns ranging from 10% to 200% per month; (3) accepting investments and distributing payouts via bank, VC exchange, e-money, remittance company, or face-to-face; (4) confirmation of investments via social media; and (5) use of VCs to justify the schemes' earning capacity.
- The entity that raised funds via an unlicensed ICO resorted to the conduct of orientation seminars to raise investor interest in the offering. The entity was represented as a foreign exchange trading club whose founder allegedly developed a new system to invest in the club's trades, resulting in the creation of a new cryptocurrency. The cryptocurrency was marketed as similar to bitcoin and was promised to experience dramatic appreciation in the next few months.

the arrest, the VC exchange's systems flagged suspicious account activities, transactions, and individuals associated with the scheme, leading to the filing of STRs on the group and their associates/cohorts.

**Unregistered ICO/Sale of VC.** In January 2018, the SEC issued its first Cease and Desist Order (CDO) against a group of related companies<sup>31</sup> publicly soliciting investments online for an ICO of tokenized shares. Allegedly, the tokenized shares, which would be purchased using VC, will be used as a medium of exchange in a technology-based agricultural marketplace. The SEC found that these tokenized shares satisfied the definition of securities in the SRC and of investment contracts based on the 4 elements of the Howey Test<sup>32</sup>. The respondents raised the following counterarguments: (1) the ICO is outside the jurisdiction of SEC as the issuing entity is not a domestic corporation; (2) the tokenized shares are not securities as these will be used as a medium of exchange and will derive their value from the owners' use rather than the efforts of others; and (3) the entity is conducting an online global offering and as such is accessible but not necessarily sold in the Philippines. Nonetheless, the SEC maintained its ruling and stated that all sales of security tokens where the buyer is located within the Philippines falls under the jurisdiction of the SEC even if the offering entity is located abroad. Likewise, the SEC clarified that when the introduction of a security is coupled with a promise of price appreciation which induces the public to purchase, such VCs are considered as securities within the definition of the SRC.

## VI. CONCLUSION

The BSP's establishment of a regulatory framework for VC exchanges has strengthened safeguards against risks associated with VCs, such as controls on anti-money laundering and terrorist financing, technology risk management, and consumer protection. In particular, the inclusion of VC exchanges as Covered Persons (CPs) has allowed for more comprehensive monitoring of the financial behavior of individuals and entities possibly connected to illicit activities as well as closer coordination and information sharing among CPs in the conduct of AML surveillance, as gleaned from the narratives submitted by the VC exchanges.

The prevalence of fraudulent activities using VC exchanges as a channel may be curbed through measures such as: (1) the imposition of lower thresholds for the amount, volume, and/or frequency of transactions that take place in an account; (2) more stringent Know Your Customer (KYC) procedures; (3) stricter requirements for increasing an account's transaction thresholds; (4) constant advisories and reminders to account holders on prohibited activities and possible penalties; and (5) more rigid AML/due diligence standards for VC exchanges' payment partners, such as remittance centers or mobile payment systems (as it was noted that a considerable number of the suspicious transactions tagged by the VC exchanges were extracted by the criminals through these channels). In addition to the strengthening of internal controls, the public's level of financial literacy must also be addressed via the conduct of learning programs to educate the public in performing their own due diligence and sense-checks when faced with financial decisions, especially in assessing investment opportunities. Finally, the passage of legislations such as the National Identification (ID) System Bill and the SIM Card Registration Bill may aid in curbing the anonymity exploited by criminals in the conduct of illicit activities.

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<sup>31</sup> The companies shared the same incorporator/founder, whose company was involuntarily delisted from the stock exchange weeks prior due to non-disclosure of material information, which also resulted in the individual's permanent disqualification from holding an officer or director position in any listed company.

<sup>32</sup> The Howey Test originated from the 1946 United States (US) case of SEC v. W.J. Howey Co., where an investment contract was defined as a "contract, transaction, or scheme whereby a person invests money in a common enterprise expecting profits to accrue solely from the efforts of the promoter or third parties."

Source: <http://sc.judiciary.gov.ph/jurisprudence/2008/feb2008/164182.htm# ftn22>, accessed on 8 August 2018